

Office of the State Auditor
Division of State Audit

Information Technology
Department
Bismarck, North Dakota

Audit Report for the
Two-Year Period Ended June 30, 2006
Client Code 112

Robert R. Peterson
State Auditor



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Transmittal Letter

August 20, 2007

The Honorable John Hoeven, Governor
Members of the North Dakota Legislative Assembly
Ms. Lisa Feldner, CIO, Information Technology Department

We are pleased to submit this audit of the Information Technology Department for the two-year period ended June 30, 2006. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

The in-charge auditor for this audit was Michael W. Schmitcke, CPA. Richard Fuher, CPA, and Angela Sabot were the staff auditors. Cindi Pedersen, CPA, was the audit supervisor. Inquiries or comments relating to this audit may be directed to the audit supervisor by calling (701) 328-4743. We wish to express our appreciation to Ms. Feldner and her staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

Robert R. Peterson
State Auditor

Executive Summary

INTRODUCTION

With the rapid change in technology and with limited resources available, it is imperative that the state's information technology professionals work together. The Information Technology Department (ITD) is established with the responsibility for all wide area network services planning, selection, and implementation for all state agencies, including institutions under the control of the State Board of Higher Education, counties, cities, and school districts. In exercising its powers and duties, ITD is responsible for computer support services, software development, statewide communications services, standards for providing information to other state agencies and the public through the internet, technology planning, process redesign, and quality assurance. It is ITD's responsibility to create alliances with agencies when implementing information technology.

RESPONSES TO LAFRC AUDIT QUESTIONS

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies.

1. What type of opinion was issued on the financial statements?

Financial statements were not prepared by the Information Technology Department in accordance with generally accepted accounting standards so an opinion is not applicable. The agency's transactions were tested and included in the state's basic financial statements on which an unqualified opinion was issued.

2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?

Other than our finding addressing "noncompliance with state procurement guidelines" (see page 25), the Information Technology Department was in compliance with significant statutes, laws, rules, and regulations under which it was created and is functioning.

3. Was internal control adequate and functioning effectively?

Other than our findings addressing the "security roles control weakness" (see page 18), "segregation of duties over accounts receivable" (see page 19), "purchase card controls weakness" (see page 20), "payroll controls weakness" (see page 21), "inventory controls weakness" (see page 22), and "computer access controls weakness" (see page 23), we determined internal control was adequate.

4. Were there any indications of lack of efficiency in financial operations and management of the agency?

There were not any indications of a lack of efficiency in financial operations and management of the Information Technology Department, although in our operational work addressing "North Dakota state portal analysis" (see page 26), we did note an area where greater efficiency could be achieved.

5. Has action been taken on findings and recommendations included in prior audit reports?

Other than the recommendation noted on page 28, the Information Technology Department has implemented all recommendations included in the prior audit report.

6. Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.

Yes, a management letter was issued and is included on page 29 of this report, along with management's response.

LAFRC AUDIT COMMUNICATIONS

1. Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.

There were no significant changes in accounting policies, no management conflicts of interest were noted, no contingent liabilities were identified or significant unusual transactions.

2. Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.

The Information Technology Department's financial statements do not include any significant accounting estimates.

3. Identify any significant audit adjustments.

Significant audit adjustments were not necessary.

4. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

5. *Identify any serious difficulties encountered in performing the audit.*

None.

6. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

7. *Identify any management consultations with other accountants about auditing and accounting matters.*

None.

8. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance, Human Resource Management System (HRMS), Data Processing Billing System, Telecommunication Billing System, Customer Information System, and 4D System are high-risk information technology systems critical to the Information Technology Department.

Background Information

The mission of the Information Technology Department (ITD) is to provide leadership and knowledge to assist their customers in achieving their mission through the innovative use of information technology. The Chief Information Officer for ITD is Lisa Feldner, who is appointed by the Governor.

ITD operates under six guiding principles: 1) ITD treats everyone with dignity and respect; 2) ITD recognizes that success depends on partnerships and collaboration; 3) ITD strives to develop quality solutions that best address the needs of our state and they are committed to delivering results – on time and within budget; 4) ITD builds long-term lasting relationships through mutual trust, and values open, honest, two-way communication; 5) ITD encourages initiative and creativity and is committed to investing in knowledge and expertise; and 6) ITD holds themselves accountable for a positive customer experience.

ITD exists for the sole purpose of leading state agencies in discovering, assessing, and implementing information technologies. ITD is committed to better understanding state agency needs and in assisting in the implementation of the proper technology solution to accomplish these needs. This is accomplished by investing in the development of highly skilled employees along with contracting outside vendors who maintain a level of expertise that is not available in-house or is limited due to the demands for a particular service.

The Information Technology Department includes eight divisions:

- Customer Services
 - Human Resources
 - Policy and Planning
 - Administrative Services
 - Software Development
 - Computer Systems
 - Telecommunications
 - Division of Independent Study
-

ITD is made up of eight divisions. Customer Services is responsible for coordinating ITD's people, process, and technology in a way that promotes customer-centric services. The Human Resources Division provides a variety of services to ITD including the recruitment, selection, and retention of highly qualified employees. The Policy and Planning Division assists state agencies with setting direction and achieving results so that the state maximizes the value from its investment in technology on a statewide basis. The Administrative Services Division includes accounting, contingency planning, security, and records management. Software Development Services is in charge of the development and maintenance of computerized applications and project management services. The Computer Systems Division provides a technical computing infrastructure and the expert skills required to host our customer's applications. The Telecommunications Division provides a variety of services to government and education. The Division of Independent Study provides distance education courses for students in grades 4-12. More information can be obtained from the North Dakota Division of Independent Study's home page at: <http://www.ndisonline.org/>

ITD's budget for the 2005-2007 biennium totaled \$109,407,227. This represents a 1.9% increase over the 2003-2005 budget. The state general funds comprise \$9.97 million of the 2005-2007 budget.

The Department is funded through a process of defining and assessing a fair and equitable billing structure for services that provides for payback of the initial investments and ongoing operations. This is accomplished by determining the actual cost of providing a specific service and establishing a unit rate for that service. More information about the agency can be obtained from the ITD's home page at: <http://www.nd.gov/itd/>

Audit Objectives, Scope, And Methodology

Audit Objectives

The objectives of this audit of the Information Technology Department for the two-year period ended June 30, 2006 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the most important areas of the Information Technology Department's operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to the Information Technology Department and are they in compliance with these laws?
3. Are there areas of the Information Technology Department's operations where we can help to improve efficiency or effectiveness?

Audit Scope

This audit of the Information Technology Department for the two-year period ended June 30, 2006 was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. To meet the objectives outlined above, we:

Audit Methodology

- Prepared financial statements from the legal balances on the state's accounting system tested as part of this audit and the audit of the state's Comprehensive Annual Financial Report and reviewed management's discussion and analysis of the financial statements.
- Performed detailed analytical procedures for expenditures and receipts.
- Tested samples of expenditures, journal vouchers, and correcting entries.
- Reviewed prior year audit workpapers.
- Interviewed appropriate agency personnel.
- Reviewed the Information Technology Department's written plans and applicable manuals.
- Observed the Information Technology Department's processes and procedures.
- Reviewed North Dakota Century Code chapter 54-59 and the 2003 and 2005 Session Laws.
- Conducted a review of the Data Processing Billing System, Telecommunication Billing System, Customer Information System, and 4D System.
- Searched for recent studies or reports relating to the Information Technology Department.

Management's Discussion And Analysis

The accompanying financial statements have been prepared to present the Information Technology Department's revenues and expenses on the legal (budget) basis. The accompanying financial statements are not intended to be presented in accordance with generally accepted accounting principles (GAAP).

The following management discussion and analysis was prepared by the Information Technology Department's management. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of this supplementary information to ensure it does not conflict with the knowledge we gained as part of our audit.

For the two-year period ended June 30, 2006, operations of the Information Technology Department were primarily supported by revenue receipts from the agency's services. This was supplemented by appropriations from the state's general fund.

FINANCIAL SUMMARY

The Information Technology Department (ITD) operates as an internal service fund. ITD tracks and monitors the cost and revenue of each service in cost centers to ensure that one service is not subsidizing another. The federal government does not allow state central service agencies to accumulate an excess fund balance. Regulations establish specific standards for determining allowable costs for services in federally funded projects. ITD monitors the cost centers and adjust rates accordingly.

Revenues remained constant - decreasing only slightly. Total revenues were \$38,488,368 for the year ended June 30, 2006 as compared to \$38,864,124 for the year ended June 30, 2005, which is a decrease of less than 1%. Computer services revenue increased \$4,222,433 from 2005 to 2006. This was due to increased usage of ITD's software development services, new revenue for ConnectND hosting, new revenue for PowerSchool hosting for K-12 schools, and increased usage of consolidated services. Revenue transfers decreased by \$4,913,918 since all the remaining revenues from the Connect ND bond were received in 2005.

Total expenses were \$45,351,059 for the year ended June 30, 2006 as compared to \$42,191,287 for the year ended June 30, 2005, which is an increase of about 8%. The increase in expenses occurs in four main areas. Salaries and wages

increased by \$1,289,731 due to increased staffing levels and normal compensation increases, both authorized by the 2005 Legislative Session. Payments to IT consultants decreased by \$3,085,662 from 2005 to 2006 due to the Connect ND project being completed in fiscal year 2005. Expenses for IT Software increased by \$2,434,038 due to rising software maintenance costs and initial software purchases related to various IT projects including ITD's mainframe migration project and the deployment of the CJIS Hub. Finally, in 2006 ITD began to make payments related to the ConnectND bond which increased expenses by \$2,704,035 from 2005 to 2006.

In addition to ITD's traditional role of providing services to customers on a charge back basis, the 2001 Legislative Session expanded ITD's responsibility to oversee several general funded technology programs. A brief description of these programs follows.

The Division of Independent Study was established in 1935 by the North Dakota Legislative Assembly to provide distance education courses for students in grades K-12 and adults. It is regionally accredited by the North Central Association Commission on Accreditation and School Improvement (NCA CASI) and is a member of the University Continuing Education Association (UCEA). The Division of Independent Study offers a broad curriculum of elementary, middle level, and high school distance education courses free of time and place constraints, enhanced through the use of new instructional technologies and delivery systems. The Division of Independent Study currently offers 181 courses for grades 4 through 12 and more than 99 courses are available online. During 2004-2005, 5,662 students were enrolled in 12,194 courses from 49 states and 29 foreign countries. More information can be obtained from the North Dakota Division of Independent Study's home page at: www.ndisonline.org/.

Senate Bill 2251 of the fifty-seventh legislative assembly created the Education Technology Council (ETC) as an entity within ITD to coordinate educational technology initiatives for elementary and secondary education. More information can be obtained from the Information Technology Department's home page: www.ndetc.k12.nd.us.

EduTech provides technical support and services to K-12 users of STAGEnet and is responsible for professional development of K-12 administrators and teachers in the use of technology to improve teaching and learning. More information can be obtained at www.edutech.nodak.edu.

A specific general fund appropriation was given to ITD to support the deployment and operation of STAGEnet to the K-12 schools throughout the state. The general funds cover the costs not funded by the Federal E-Rate Program.

A specific general fund appropriation was given to ITD to support the deployment and operation of a centralized Geographic Information System (GIS) hub to make data more easily available and reduce costs by pooling the resources and data used by all levels of government.

A specific general fund appropriation was given to ITD to support the deployment and operation of a centralized Criminal Justice Information Sharing (CJIS) hub to make data more easily available and reduce costs by pooling the resources and data used by all levels of law enforcement agencies.

ACCOMPLISHMENTS/INITIATIVES

StageNet usage continues to grow. ITD spent a significant amount of effort designing the specifications for the state network infrastructure required to support customer requirements over the next several years. ITD awarded contracts for the next generation of StageNet services and cut over to the enhanced network was completed in December of 2006.

ITD's second data center came online in early 2006. ITD previously contracted for hot site services in Colorado. The processing and bandwidth capacity requirements of the current data center have grown and it was cost prohibitive to contract for the required capacity. The second data center allows ITD to provide redundant hardware for those customers who require fail over processing capacity and allows ITD to recover critical systems within 8 hours of disaster as compared to our previous recovery windows of 48-72 hours.

The new ND.GOV portal has a redesigned interface and has improved the ability of citizens to access government information and utilize e-government services.

Our traditional help desk was transformed into a customer focused "service desk" that combines interpersonal skills, technical expertise, and business awareness. This new breed of support structure not only handles incidents and questions, but also provides an interface for other business activities, including customer work orders, requests for change, problem root-cause analysis, and service level management.

The CJIS hub grew significantly in 2005, with 826 users registered for access. Over 560,000 transactions occurred for fiscal year 2005. New enhancements to the hub included the ability to check

offenses on non-sufficient funds, search capabilities of central warrant information systems, search capabilities of custody and supervision records, and the addition of the offender registration report.

The GIS Technical Committee (GISTC) continues to enhance the GIS Hub by adding data and applications and increasing awareness of the Hub by promoting its use, value, and functionality. These efforts continue to pay off as indicated by the usage of the GIS Hub. There is an average of 35-40 daily concurrent connections to the GIS Hub database from state agencies. The web applications average over 70,000 hits per month compared to an average of 50,000 hits during the previous year. April 2006 was a record-setting month for the GIS Hub web applications with over 102,000 hits. Data downloads average over 2,800 per month.

North Dakota schools continue to benefit from the centralized internet filter, purchased and managed by EduTech, which makes it possible for them to comply with the Children's Internet Protection Act (CIPA) technology requirements and corresponding E-Rate regulations.

ITD publishes an annual report that discusses our major IT accomplishments in more detail. The report can be found at www.nd.gov/itd/pubs.

FUTURE CRITICAL ISSUES

ITD is committed to a process of continuous improvement with a primary focus on customer service. We have added a new guiding principle to "hold ourselves accountable for a positive customer experience." This customer-centric focus is critical as we continue to challenge our staff and analyze our business processes to improve on managing customer expectations and providing a positive customer experience.

ITD's greatest asset is the knowledge and abilities of our staff. We make considerable investments in equipping our employees to perform their jobs. Over the past year ITD has started to see an increase in our voluntary turnover rate. This increase, coupled with recent compensation studies indicating there is widening gap between state compensation and the private sector compensation is of significant concern to our Department. This trend comes at a time where we are seeing an increasing demand from our customer base for ITD services.

Accordingly, recruiting, developing, and retaining a top-notch technology staff continue to be a focus for the ITD management team. In addition, we are working with interim legislative committees to discuss compensation issues in state government

and innovative ways to address employee compensation and retention.

Industry trends continue toward using Voice over Internet Protocol (VoIP) to reduce communication costs and enhance services. ITD has started migrating portions of our infrastructure to take advantage of this technology. The migration to this technology is expected to continue through the 2009-2011 biennium.

Information technology security and related privacy issues remain critical issues in the operation of STAGEnet, the continued expansion of e-government services and the Criminal Justice Information Sharing System. ITD will need to provide expertise and leadership in working with state agencies to help the state adequately secure its information technology resources.

We have been encouraged by the level of agency participation in the Enterprise Architecture process. Continued participation by state agencies and higher education in the enterprise architecture has many benefits. It helps ensure that IT investments are ultimately helping agencies fulfill their mission. It connects the selection, creation, and implementation of IT solutions to specific business purposes. Enterprise architecture assures policy-makers that agencies are creating new systems and eliminating old ones through a consistent process.

Financial Statements

STATEMENT OF REVENUES AND EXPENSES

	June 30, 2006	June 30, 2005
<u>Revenues and Other Sources:</u>		
Computer Services	\$ 35,522,034	\$ 31,299,601
Sale of Publications	1,147,672	989,912
Student Fees	1,132,621	1,065,087
Telecommunications Relay Service	429,778	416,527
Miscellaneous Revenue	256,263	179,079
Transfers In		4,913,918
Total Revenues and Other Sources	\$ 38,488,368	\$ 38,864,124
<u>Expenditures and Other Uses:</u>		
Salaries and Benefits	\$ 15,628,883	\$ 14,339,152
Other Capital Payments	2,704,035	
IT Equipment over \$5,000	1,834,041	1,296,616
Grants, Benefits, and Claims	1,536,517	1,914,450
Equipment over \$5,000	51,240	51,488
Major Operating Expenses:		
IT Contractual Services	9,243,041	12,328,703
Supplies – IT Software	7,545,897	5,111,859
IT – Communications	2,833,664	2,825,077
Repairs	727,334	553,079
IT Equipment under \$5,000	616,878	659,244
Rent of Building Space	560,308	469,885
Office Supplies	455,694	354,756
Professional Development	341,720	427,246
IT – Data Processing	303,080	804,979
Travel	273,256	229,645
Other Operating Expenses	695,470	825,106
Total Expenditures and Other Uses	\$ 45,351,059	\$ 42,191,287

STATEMENT OF APPROPRIATIONS

For The Fiscal Year Ended June 30, 2006

Expenditures by Line Item:	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Salaries and Wages	\$ 29,327,174	\$ 354,000	\$ 29,681,174	\$ 13,548,368	\$ 16,132,806
Operating Expenses	48,908,146	146,000	49,054,146	20,386,656	28,667,490
Capital Assets	10,361,163		10,361,163	4,540,403	5,820,760
Independent Study	6,016,779		6,016,779	2,575,544	3,441,235
Education Technology Grants	886,597		886,597	316,152	570,445
Edu Tech	2,652,348		2,652,348	1,357,572	1,294,776
Wide Area Network	7,542,950		7,542,950	1,723,638	5,819,312
Geographic Info. System	686,980		686,980	322,266	364,714
Criminal Justice Information	2,525,090		2,525,090	510,653	2,014,437
Totals	<u>\$108,907,227</u>	<u>\$ 500,000</u>	<u>\$109,407,227</u>	<u>\$ 45,281,252</u>	<u>\$ 64,125,975</u>
Expenditures by Source:					
General Fund	\$ 9,972,837		\$ 9,972,837	\$ 4,920,557	\$ 5,052,280
Other Funds	98,934,390	\$ 500,000	99,434,390	40,360,695	59,073,695
Totals	<u>\$108,907,227</u>	<u>\$ 500,000</u>	<u>\$109,407,227</u>	<u>\$ 45,281,252</u>	<u>\$ 64,125,975</u>

Appropriation Adjustments:

Emergency Commission Request number 1576 increased the Information Technology Department's spending authority for salaries and wages by \$354,000 and operating expenses by \$146,000. The increases were to cover the additional costs associated with the transition of developer functions that used to be performed by the Bank of North Dakota that will now be performed by the Information Technology Department.

For The Biennium Ended June 30, 2005

Expenditures by Line Item:	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Salaries and Wages	\$ 25,715,694	\$ (500,000)	\$ 25,215,694	\$ 24,593,771	\$ 621,924
Operating Expenses	32,120,860	2,482,668	34,603,528	33,058,905	1,544,623
Capital Assets	5,323,000	(250,000)	5,073,000	3,386,852	1,686,148
Independent Study	5,625,480		5,625,480	4,645,096	980,384
Education Technology Grants	793,818		793,818	784,322	9,496
Sendit Network	-	2,540,348	2,540,348	2,540,348	
Wide Area Network	7,436,223		7,436,223	3,612,141	3,824,082
ERP System	20,000,000		20,000,000	18,889,812	1,110,188
Geographic Info System	678,343		678,343	578,857	99,486
Prairie Public Broadcasting	1,337,138		1,337,138	1,337,138	
Criminal Justice Information	4,741,200	(650,000)	4,091,200	221,383	3,869,817
Edu Tech	2,540,348	(2,540,348)			
Totals	<u>\$106,312,104</u>	<u>\$ 1,082,668</u>	<u>\$107,394,772</u>	<u>\$ 93,648,625</u>	<u>\$ 13,746,147</u>
Expenditures by Source:					
General Fund	\$ 8,194,803	\$ 1,070,142	\$ 9,264,945	\$ 9,192,015	\$ 72,930
Other Funds	98,117,301	12,526	98,129,827	84,456,610	13,673,217
Totals	<u>\$106,312,104</u>	<u>\$ 1,082,668</u>	<u>\$107,394,772</u>	<u>\$ 93,648,625</u>	<u>\$ 13,746,147</u>

Appropriation Adjustments:

The EduTech line item is the same as the Sendit Network line item. ITD's 2001-2003 budget included a line item for Sendit (Line 73). Sendit changed their name to EduTech. OMB was unaware of the name change and when the 2003-2005 budget referenced EduTech they initially created a new line item (Line 79). ITD notified OMB of the name change and OMB transferred the appropriation authority from Line 79 to Line 73 and changed the name of the line item from Sendit to EduTech.

A portion of the Salaries and Wages, Capital Assets, and Criminal Justice Information System line item appropriation authorities were transferred to the Operating Expenses line item to cover additional operating expenses. The line item transfers were authorized by House Bill 1505, section 9, of the Fifty-eighth Legislative Assembly.

The Emergency Commission approved the Information Technology Department's increased spending authority for operating expenses by \$12,526. The increase was to accept federal funds from the United States Department of Justice for spending related to the criminal justice information system.

House Bill 1015, section 3 of the Fifty-ninth Legislative Assembly approved a deficiency appropriation in which \$1,070,142 of additional spending authority was transferred to the Information Technology Department's operating expenses line item.

Internal Control

In our audit for the two-year period ended June 30, 2006, we identified the following areas of the Information Technology Department's internal control as being the most important:

Internal Controls Subjected To Testing

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenditures.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.
- Controls surrounding the computer-based Data Processing System, Telecommunication System, Customer Information System, and 4D.

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered significant. We concluded that internal control was not adequate noting certain matters involving internal control and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect the Information Technology Department's operations or ability to record, process, summarize, and report financial data consistent with the assertions of management in financial statements. Reportable conditions are described below. We also noted other matters involving internal control that we have reported to management of the Information Technology Department in a management letter dated August 20, 2007.

SECURITY ROLES CONTROL WEAKNESS

Finding 06-1

The security roles used by the Information Technology Department had a design flaw which resulted in a significant internal control weakness. As a result, individuals with the role to approve expenditure transactions also had the ability to initiate the same transactions. Proper internal controls dictate that these two functions be separated. The Office of Management and Budget is responsible for these security roles. OMB has redefined these roles during our audit period so no recommendation will be made to ITD.

Finding 06-2

SEGREGATION OF DUTIES OVER ACCOUNTS RECEIVABLE

The Information Technology Department has not properly segregated duties related to their accounts receivable function. Individuals with access to cash were also responsible for posting debits and credits to accounts receivable records. Additionally, individuals charged with the responsibility of approving write-offs and adjustments to accounts receivable records also had access to make adjustments to the accounts receivable records. The lack of segregation of duties within the accounts receivable function has increased the risk of errors going undetected, fraudulent activity occurring, and data being corrupted.

To limit the Department's exposure to the risks noted above, proper segregation of duties is critical. Individuals with access to cash or are charged with the responsibility for approving write-offs and adjustments to accounts receivable records should not be responsible for posting adjustments to or have access to update accounts receivable records.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Information Technology Department properly segregate duties to ensure individuals with access to cash and individuals responsible for approving write-offs and adjustments to accounts receivable records do not have the responsibility or access to update accounts receivable records.

Information Technology Department Response:

We agree with the recommendation and will implement changes to our existing business processes to mitigate this risk.

PURCHASE CARD CONTROLS WEAKNESS

Internal controls surrounding the Information Technology Department's purchase card activity are inadequate.

We noted instances where:

- Cardholders were not reconciling their individual purchase card statements to the receipts and not signing the statement to attest that all purchases were for state business and that they complied with all applicable rules and regulations;
- Purchase card expenditures were not being approved;
- Receipts were not kept for purchases made and/or the purchase card statement was not kept; and
- Agency-wide purchase card statements were not reconciled to individual purchase card statements.

The Office of Management and Budget's (OMB) Fiscal and Administrative Policy 300 and additional guidance provided by OMB identifies the controls that are required to be implemented by agencies using a purchase card. The policy requires cardholders to reconcile their individual purchase card statements to receipts, purchase card expenditures be approved, receipts to be attached to the individual purchase card statement, and agency-wide purchase card statements be reconciled to individual purchase card statements. In the absence of these controls the risk of erroneous or fraudulent purchases occurring is greatly increased.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Information Technology Department implement controls in accordance with OMB guidance and OMB Fiscal and Administrative Policy 300, and at a minimum ensure: cardholders reconcile their individual cardholder statement to receipts and sign and date the statement; purchase card expenditures are approved and signed by the approver; all receipts are attached to the individual purchase card statement; and individual purchase card statements are reconciled to the agency wide statement.

Information Technology Department Response:

We agree with the recommendation. While we do have existing controls that include our p-card administrator reconciling all individual statements to the agency-wide statement and to PeopleSoft, we will incorporate these recommendations into our business processes.

PAYROLL CONTROLS WEAKNESS

We identified two control weaknesses surrounding ITD's payroll process.

1. One-time payments to employees which are entered into PeopleSoft are not being properly approved.
2. Hours worked by hourly employees are not being approved.

The weaknesses noted above enable unauthorized payroll payments and adjustments to be made and go undetected as well as hourly employees being paid for hours not worked. To eliminate these risks it is imperative that all one-time payments are approved by an individual who does not have access to process payroll and all hours worked by hourly employees be approved.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Information Technology Department implement controls to ensure all one-time payments entered into PeopleSoft are approved by an individual who does not have access to process payroll and all hours worked by hourly employees are approved.

Information Technology Department Response:

We agree with the recommendation. We will change our business process to include formal approval of hourly employee's timesheets. While we do have existing controls surrounding one-time adjustments we will change the current approval process to mitigate the risks identified in this recommendation.

Finding 06-5

INVENTORY CONTROLS WEAKNESS

The Information Technology Department does not properly restrict access to inventory items located within the department. Also, the locations of inventory items listed in the inventory records are not kept current.

Of the 5,899 items totaling approximately \$28.8 million, we tested 37 items to determine if the items listed in the inventory records existed. Our results showed that of the 37 items selected 12 of the items had the incorrect location listed in the inventory records and 2 items were not found. The 2 items not located were a 19-inch computer monitor and a laptop computer.

ITD has several rooms within the Department that are used to store computer equipment such as laptops and monitors. The equipment is used by ITD employees on an as needed basis. However, there are no procedures in place to monitor who takes the equipment and its location or to ensure that the equipment is returned.

In order to prevent items from being misplaced or stolen it is imperative that access to inventory items be properly restricted and ensure inventory records are kept current.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Information Technology Department implement controls to ensure access to inventory items be restricted to the proper individuals and that all inventory locations listed in the inventory records be kept current.

Information Technology Department Response:

We agree with the recommendation and will implement more formal procedures surrounding the deployment of our inventory items.

COMPUTER ACCESS CONTROLS WEAKNESS

The Information Technology Department and Division of Independent Study employees have access rights to 4D (tracks student accounts including courses being taken and payments made), Customer Information System, and PeopleSoft's financial environment which are not necessary to perform their normal job duties. Our review noted the following critical issues:

- Employees have access to PeopleSoft modules not currently used by the Department;
- Employees approving transactions have access to add, delete, and update records;
- Employees have access to the Customer Information System, but do not have any job duties related to the system;
- Employees taking annual inventories also have access to computerized fixed asset records; and
- All financial personnel at the Division of Independent Study have unlimited access to the student accounts including making adjustments, posting debits and credits to student accounts, and modifying account information.

Proper internal control dictates that access to data be limited to those who require access to perform their duties. Employees who approve transactions should not have access to process transactions. Without proper access controls, personnel have the opportunity to bypass many important controls, especially segregation of duties. Therefore, there is an increased risk of unauthorized transactions and also a greater chance of corruption of data.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Information Technology Department and Division of Independent Study properly restrict access to the various roles or areas in 4D, Customer Information System, and PeopleSoft's financial environment to only those individuals who require access to perform their normal job duties and assign maintaining security for each system to an individual. The individual should perform a review of all access rights on at least an annual basis to ensure that the access is appropriate based on the job duties of the personnel.

Information Technology Department Response:

We agree with the recommendation and will strengthen our controls surrounding access to the identified systems.

Compliance With Legislative Intent

In our audit for the two-year period ended June 30, 2006, we identified and tested the Information Technology Department's compliance with legislative intent for the following areas that we determined to be significant and of higher risk of noncompliance:

Legislative Intent Subjected To Testing

- Policies, standards, and guidelines established by the Advisory Committee (NDCC section 54-59-02.1).
- Salary of the Chief Information Officer (NDCC section 54-59-03).
- Compensation for State Information Technology Advisory Committee members (NDCC section 54-59-07).
- Deposit of monies into the Information Technology Fund (NDCC section 54-59-17).
- Calculation of the telephone access line surcharge rate (NDCC section 54-44.8-08 subsection 1).
- Compliance with appropriations and related transfers (2003 North Dakota Session Laws chapter 665 of the Special Supplement sections 1 and 7, and 2005 North Dakota Session Laws chapters 49 and 13 sections 6 and 7 and 4 and 5, respectively)
- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with OMB's Purchasing Procedures Manual.
- Travel-related expenditures are made in accordance with OMB policy and state statute.
- Proper use of outside bank accounts.
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with fixed asset requirements including record keeping, surplus property, lease and financing arrangements in budget requests, and lease analysis requirements.
- Compliance with payroll related laws including statutory salaries for applicable elected and appointed positions, and certification of payroll.

The results of our tests disclosed one instance of noncompliance that are required to be reported under *Government Auditing Standards*. This finding is described on the following page. Other than that finding, we concluded there was compliance with the legislative intent identified above. We also noted certain immaterial instances of noncompliance that we have reported to management of the Information Technology Department in a management letter dated August 20, 2007.

Finding 06-7

**NONCOMPLIANCE WITH STATE PROCUREMENT
GUIDELINES**

The Information Technology Department purchased commodities or services without complying with the Office of Management and Budget's State Procurement Guidelines.

State Procurement Guidelines require agencies to obtain three oral or written informal bids or provide a written explanation why three bids were not obtained for purchases of commodities or services from \$2,500 to \$25,000. Eight instances were noted where the Information Technology Department procured items without obtaining the minimum number of bids, failed to document why three bids were not obtained, and procured services based on an outdated contract.

Failure to follow State Procurement Guidelines can result in the State paying more for commodities and services than is necessary and also lead to inappropriate purchases being made from vendors in which Department employees have an interest.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Information Technology Department comply with the Office of Management and Budget's State Procurement Guidelines.

Information Technology Department Response:

We agree with the recommendation. We make every attempt to comply with OMB's procurement guidelines and policies and will improve our business processes in this area.

Our audit of the Information Technology Department identified the following areas of potential improvements to operations:

Operational
Improvement 06-1

NORTH DAKOTA STATE PORTAL ANALYSIS

Point of Interest:

Technology has become integral to the success of nearly every facet of government and in the services it delivers to citizens. As society has grown more complex, governments have received increased pressure to deliver high-quality services at a reasonable cost. EGovernment has emerged as one of the key ways governments can meet this demand. Listed below are some critical EGovernment services and types of information that could be provided or improved by ITD on the North Dakota state portal.

What we found:

- The Information Technology Department has developed the ND state portal and included numerous online services for citizens to use to do business with the state. However, there continues to be a number of critical online services not currently available on the ND state portal that should be developed by ITD in conjunction with the applicable state agency. Some of the online services that should be developed are listed below:
 - State parks and campsite reservations, criminal history background checks, vehicle identification number validating search, Uniform Commercial Code Filings, social services benefits application and status checking, child support billing and payment information, adoption/foster parent application, business registration renewal, online procurement services, and online applications for government jobs.
- Online registrations for occupational and professional licenses are available through many state agency websites. However, the licenses listed on the ND state portal were not complete, could not be sorted, and did not provide links to the licensing entity.
- E-forms listed on the ND state portal are not searchable by category nor were the most commonly used forms listed in a drop down box as they are in other top ranking states reviewed, making it difficult for users to find the applicable e-form.

- Additional information noted on other top ranking state portals that are not included on the ND state portal are:
 - Java applets for current weather information, a Kid Zone for students and kids about state government and ND's history, a news link that provides a list of current top stories for all state government including the option of using RSS feeds; and an events link that lists all current and upcoming state events of public interest.

Criteria:

There are several national surveys that review state portals and rank them. The surveys identified were the Digital States Survey and Best of the Web Survey both conducted by the Center for Digital State Government and the EGovernment Trend Report conducted by the National Policy Research Council. We used these identified best practices to determine if there were areas of the North Dakota (ND) state portal that could be improved as well as benchmark the ND state portal against other top ranking state portals to reveal other areas for potential improvement.

Operational Improvement:

We recommend the Information Technology Department work with the applicable state agencies to develop the online services discussed above, streamline the search capabilities for license applications and other e-forms, and consider including some of the additional information provided by other top ranking state portals.

Information Technology Department Response:

We appreciate the work the State Auditor's Office has done in researching ways to improve the state portal, ways to improve access to portal resources and identifying potential on-line services that might benefit North Dakota citizens. We will keep these recommendations in mind as we continue to enhance the portal. A few of the suggested on-line services are already in the development process and we will work with applicable state agencies to determine whether the remaining applications align with their strategic plans.

Prior Recommendations Not Implemented

Prior recommendations have been implemented with the exception of the following:

Background

During our review of the Customer Information System access controls, we noted the following:

- Employees approving transactions also have access to add, delete, and update records;
- Employees have access to the system, but do not have any job duties related to the system; and
- Employees taking annual inventories also have access to computerized records.

Additionally, a review of the PeopleSoft payroll access controls noted that the Information Technology Department had nine employees who had been given Superuser ID's. These Superuser ID's allow complete and unrestricted access to all aspects of the PeopleSoft payroll system.

Proper internal control dictates that access to data should be limited to those who need access to the data to perform their duties. Employees who approve transactions should not have access to process transactions and only a limited number of individuals should be permitted to have Superuser ID's. Without proper access controls, personnel have the opportunity to bypass many important controls, especially segregation of duties. Therefore, there is an increased risk of unauthorized transactions and also a greater chance of corruption of data.

Recommendation

We recommend the Information Technology Department:

- Restrict access to the Customer Information System or begin using the PeopleSoft fixed asset module to ensure that personnel have access only to the information necessary to perform their job duties and keep the approval function separated from the processing function; and
- Reduce the number of individuals who have Superuser ID's and ensure that anyone who does have a Superuser ID does not have the ability to input data into the system.

Status

The recommendation was partially implemented. Superuser ID access was adequately reduced and restricted. The Customer Information System access controls were not properly restricted. See "computer access controls weakness" on page 23.

Management Letter (Informal Recommendations)

August 20, 2007

Ms. Lisa Feldner, CIO
Information Technology Department
State Capitol
600 E Boulevard Avenue
Bismarck, North Dakota 58505

Dear Ms. Feldner:

We have performed an audit of the Information Technology Department for the two-year period ended June 30, 2006, and have issued a report thereon. As part of our audit, we gained an understanding of the Information Technology Department's internal control structure to the extent we considered necessary to achieve our audit objectives. We also performed tests of compliance as described in the same report.

Our audit procedures are designed primarily to enable us to report on our objectives including those related to internal control and compliance with laws and regulations and may not bring to light all weaknesses in systems and procedures or noncompliance with laws and regulations which may exist. We aim, however, to use our knowledge of your organization gained during our work to make comments and suggestions which we hope will be useful to you.

In connection with the audit, gaining an understanding of the internal control structure, and tests of compliance with laws and regulations referred to above, we noted certain conditions we did not consider reportable within the context of your audit report. These conditions relate to areas of general business practice or control issues that have no significant bearing on the administration of federal funds. We do, however, want to present our recommendations to you for your consideration and whatever follow-up action you consider appropriate. During the next audit we will determine if these recommendations have been implemented, and if not, we will reconsider their status as non-reportable conditions.

The following present our informal recommendations.

CASH

Informal Recommendation 06-1: We recommend the Information Technology Department develop a PeopleSoft query to identify all adjustments made to accounts receivable records, an individual who does not have access to accounts receivable records generate this report monthly, verify all adjustments are necessary and proper, and approve the report.

Informal Recommendation 06-2: We recommend the Information Technology Department implement a process to ensure all GL correcting entries are approved by an appropriate individual that is also independent of preparation.

ACCOUNTS PAYABLE/EXPENDITURES

Informal Recommendation 06-3: We recommend the Information Technology Department ensure that the individual responsible for approval in the Accounts Payable ledger on PeopleSoft use the “worklist” link on the right top of the screen in PeopleSoft when approving vouchers.

Informal Recommendation 06-4: We recommend the Division of Independent Study ensure that all their p-cards have a Merchant Category Code (MCC) Table restriction of something other than NDFRD1 (least restrictive of the four MCC tables available) and that individual p-card statements are reconciled to the agency-wide statement by a non-cardholder.

PAYROLL

Informal Recommendation 06-5: We recommend the Division of Independent Study implement procedures to ensure:

- Payroll checks are distributed by an individual who does not have access to process payroll; and
- All one-time adjustments are adequately reviewed and approved by an individual independent of payroll preparation.

LEGISLATIVE INTENT

Informal Recommendation 06-6: We recommend the Information Technology Department ensure the individuals taking the annual physical inventory do not have access to the fixed asset records and sign off on the inventory to certify its correctness in accordance with NDCC 44-04-07.

Informal Recommendation 06-7: We recommend the Information Technology Department ensure that the Office of Management and Budget Fiscal and Administrative Policy 214 – Crediting Appropriations is followed.

Informal Recommendation 06-8: We recommend the Information Technology Department obtain approval for shadow systems that they believe must be maintained since the implementation of ConnectND.

OPERATIONAL

Informal Recommendation 06-9: We recommend the Information Technology Department participate in the Best of the Web contest and enter accurate information into the Digital States Survey.

Informal Recommendation 06-10: We recommend ITD develop procedures and assign responsibility to ensure all information on the portal and their website is kept current.

GENERAL

Informal Recommendation 06-11: We recommend the Division of Independent Study create a report in 4D that will identify all credit memos and ensure the report is generated, reviewed, and approved by an individual that does not have access to make adjustments or write-offs to accounts in 4D.

Informal Recommendation 06-12: We recommend the management of the Information Technology Department take an active role in the development and monitoring of internal controls surrounding critical business functions to ensure internal controls are operating efficiently and effectively.

Management of the Information Technology Department agreed with these recommendations.

I encourage you to call myself or an audit manager at 328-2243 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,

Michael W. Schmitcke, CPA
Auditor in-charge